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TAGS: [ECON](#) [ECONOMY](#) [AND](#) [FINANCE](#) [ISRAELI](#) [SOCIETY](#) [GOI](#) [INTERNAL](#)

SUBJECT: POVERTY HYPE REFLECTS DECLINE OF SOCIALISM IN
ISRAEL

Classified By: Charge d'Affaires Gene A. Cretz for reasons 1.05 (b and d).

Summary

1. (S) In advance of the upcoming elections, many politicians, reporters, and advocacy groups have been trumpeting "poverty" as the most important issue facing Israeli society. In reality, apart from a few isolated pockets, Israel does not face grinding "third world-style" poverty as a systemic problem. What it does face is a slowly growing gap between the "haves" and the "have-nots," which has been exacerbated somewhat in the last two years by the implementation of the economic reform program of former Finance Minister Netanyahu. People in the lower socio-economic strata have had their government benefits cut, but the economic recovery has not yet been able to provide enough good new jobs to compensate. The recovery has been strong in high technology and finance, but anemic in traditional industries such as food and textiles keeping the unemployment rate at a still high 8.9 percent. The attacks charging Netanyahu and his reform program with responsibility for a dramatic increase in "poverty" in Israel are misleading, at best, and demagogic, at worst. They are really an attack by entrenched economic interests on Israel shifting economic priorities. These interests, primarily the labor unions and others who hearken back to Israel socialist past have lost the fight to control Israel economic future. This loss has generated a backlash, which has turned into a political battle over those who are still "left behind" by the recovery. Regardless, the furor over "poverty" is bringing attention to the growing inequality in the society, and any government formed after the March 28 election will have to address the issue. End Summary.

Inequality the Issue, Not Poverty

2. (S) The issue of "poverty" has taken center stage in the Israeli election campaign, especially since the election of Amir Peretz to head the Labor Party. Former Finance Minister Netanyahu has become a lightning rod for criticism, even from within his own political party, that his policies were "heartless" and dramatically increased poverty. Several NGOs have recently issued reports to demonstrate an increase in poverty, which the press highlighted with alarmist headlines. This has surprisingly, kept the election campaign more focused than usual on economics, even with the recent terrorist attack in Netanya and the furor over claims by a Sharon adviser that Sharon would eventually divide Jerusalem and withdraw from 90% of the West Bank. However, the true message of the poverty reports is not that many Israelis live in abject poverty, but that the gap between the "haves" and the "have-nots" has widened as wealthier sectors of society have benefited more quickly than the "poor" from the economic recovery.

Bachar Committee on Poverty Formed

3. (S) Even before Peretz election, the issue of poverty was becoming increasingly important in the Israeli political arena, to the point where then Acting Finance Minister Olmert, upon succeeding Netanyahu in office, made repeated statements about the need to increase spending to address the issue. Olmert had fully supported the Netanyahu reforms while serving in the Sharon government, but sensed that their impact on the lower socio-economic sector was becoming a major political issue. While the government has promised to continue to adhere to the Loan Guarantee Agreement terms, which call for a budget deficit maximum of three percent of GDP and a maximum increase in the rate of expenditure growth of one percent, Sharon and Olmert felt enough heat on the issue to appoint the "Bachar Committee on Poverty." The committee, named after its chairman, Finance Ministry Director General Yossi Bachar, was tasked with generating ideas on ways to alleviate poverty. The report on its conclusions was supposed to come out at the end of November, but committee member Karnit Flug, Director of the Bank of Israel Research Department, told econoff at that time that the committee had not yet completed its work. On December 18, the Committee met with the PM and the Finance Minister to discuss its preliminary findings. According to the websites of the PM and MoF, they discussed a recommendation for a seven year NIS 14 billion (\$3.04 billion) plan. The PM and FM asked the committee to devise a specific plan with timelines for implementation. In addition, they also asked to hold a meeting within the next month to discuss the possibility of adopting an earned income tax credit. (Note The PM December 18 stroke casts doubt on when/whether this meeting

will take place. End Note)

Make it Easier for People to Work

14. (C) Flug said that the committee would not recommend radical solutions, but would rather suggest incremental ways to help alleviate some of the difficulties of those who have not yet benefited from the rising economic tide, especially those whose allowances were cut, but have not yet found stable employment. The idea, she said, was to make it easier for people to join the work force, for instance, by having the government pay for child-care while a mother goes to work. The money spent would more than be made up for in the long-term by successfully integrating the beneficiary into the full-time tax-paying work force. Another controversial idea under discussion is a U.S.-style earned income tax credit, which Flug indicated is being mistakenly referred to as a "negative income tax" by the press. She said that the program success in the U.S. has brought about an examination of its applicability in the Israeli context, although many - including some in the Finance Ministry - oppose it as a bureaucratic headache, which will accomplish little.

15. (U) According to press reports, other ideas under consideration by the Bachar Committee include encouraging the building of factories in the Arab sector, providing incentives for Arab and ultra-Orthodox Jews to find jobs, increasing subsidies for training and education in underdeveloped areas, giving incentives to employers to hire new workers, increasing assistance to the elderly, and lowering health care taxes on low income wage earners. These press reports substantiate Flug contention that the committee emphasis is on finding ways to make working a more attractive option, and to move people off of allowances, rather than to return to the "culture of allowances" that had prevailed prior to the reforms.

IMF: Maintain Fiscal Discipline

16. (U) The preliminary IMF report on the Israeli economy issued on December 12 agreed with the thrust of the Bachar Committee thinking. It recognized that cuts in benefits have harmed certain groups such as the elderly and disabled, and those unable to work, and that it is necessary to retain a social safety net for their benefit. But it stressed the need to remain within the present fiscal framework, and to provide incentives that encourage people to work.

National Insurance Institute 2004 Poverty Report

17. (U) The poverty line in Israel is defined as 50% of median net income. In 2004, the line stood at NIS 1,777 (USD 386 at the present exchange rate of 4.6) per month for an individual and NIS 4,548 (USD 989) for a family of four. These figures are about 25.5 percent and 65.4 percent of average monthly income of approximately NIS 6970 (USD 1515). In August, the National Insurance Institute provided the impetus for the increased discussion of the poverty issue when it put out a report, which indicated that the number of people falling below the poverty line had risen from 1,426,800 in 2003 to 1,534,000 in 2004. In addition, it said that the number of children living in poverty increased from 652,400 to 713,600 and the number of impoverished families increased from 366,300 to 394,200 in the same time frame. These statistics say that about 22 percent of the Israeli population lives under the poverty line, up from fourteen percent in 1990, before any attempt had yet been made to rein in the welfare state. The very large number of people living beneath the poverty line now indicates that the measure used casts a very wide net, and that many people have been hurt by the cuts in government benefits. However, most of them do not live in abject poverty and will likely benefit from continued economic recovery. The National Insurance Institute is scheduled to issue updated figures soon.

Advocacy Group Says Poor Get Poorer

18. (U) In addition, the ADVA Center for Information on Equality and Social Justice in Israel will shortly come out with its annual report on the economic situation of the disadvantaged in Israel. There have been numerous leaks to the press about its contents. The report will say that the economy has experienced unbalanced growth, with investment and high wages being concentrated in only a few sectors. According to ADVA interpretation of statistics released by the government Central Bureau of Statistics, the high technology sector grew its contribution to GDP by 100% since the early 1990s, while the insurance, banking, and real estate sectors grew by 50%. In contrast, traditional industries such as food and textiles, in which many of the working poor are employed, grew by only four percent. The net result, according to ADVA, is that the rich have gotten richer and the poor poorer.

"Social" Economist Sees Severe Societal Deterioration

9. (S) In contrast to ADVA conclusions, the real message of the statistics is that there has been some temporary deterioration in the situation of those whose allowances were cut and who have not yet found jobs. However, other than amorphous anecdotal accounts, there has been no documentation to suggest that these people are suffering from true abject poverty, and that their children are going to bed hungry. In a meeting with econoff, Hebrew University "social economist" Momi Dahan, former Senior Advisor to the Finance Ministry DG, and an advocate of a strong welfare state, said that the face of Israel has changed dramatically over the past fifteen years. He described a Dickensian society where poverty is rampant, many cannot afford food, and soup kitchens are ubiquitous, saying that it reminded him very much of the United States. He gave little credit for the economic "recovery" to the reform program, but ascribed most of it to the wind-down of the intifad and the return of global prosperity. He did, however, credit Netanyahu with maintaining fiscal discipline, which he said is important. His prescription for dealing with poverty is to keep the deficit under control, but reintroduce high taxes to pay for the costs of necessary welfare programs. His main contention was that in welfare states, such as Sweden, poverty is not an issue, but that in other types of societies, such as the U.S. and Israel (now), it is. However, when asked the source of his information on the spread of soup kitchens and other such facilities, he said that the evidence is what he sees with his own eyes every day - in other words, anecdotal.

Growth Will Eventually Reach the Bottom Rungs

10. (S) Dahan illustrates the "sky is falling" atmosphere prevalent in Israel today regarding poverty. Some, such as Gil Bufman, Chief Economist at Bank Leumi, and Yossi Gordon, Deputy Budget Director at the MoF, dismissed the poverty issue out of hand in discussions with econoff. Bufman said something to the effect that an impoverished person in Israel is someone who does not own a cell phone. Gordon was similarly dismissive. Both acknowledged that the problem Dahan addresses is real, but said that his characterizations of it are exaggerated. Once the economy has the time to work through the dislocations brought about by the reforms and the new demands of the world economy, the benefits of economic growth are likely to reach those on the bottom rungs as well, whether they be Jews of North African and Middle Eastern origin, ultra-Orthodox Jews, Arabs or Druze, or the elderly.

The Fight is Over How to Divide the Pie

11. (C) The situation of most of the "poor" has remained fairly static in recent years, while the well-off have experienced a period of prosperity. However, as written on December 13 by the economics reporter for Ma riv, Moshe Perl, the issue is the need to "understand the difference between the battle to increase the size of the cake and the battle over how it is divided up. The furious socio-economic controversy taking place here now does not succeed in making that basic distinction. People who are not satisfied with the manner in which the fruits of economic growth are being divided have launched a public campaign against the very methods and the plans which made that growth possible

Under no circumstances must we do away with a policy which has made growth possible just because it emerges that its benefits are not shared as we would wish." In a December 12 ruling, the Israeli Supreme Court rejected an appeal by numerous advocacy NGOs demanding that the Court order the government to reinstate the allowances that were cut. The Court said that the country has an obligation to take care of those in need, but it is up to the elected government to decide how money should be spent.

Peretz Will Not Bust the Budget Framework

12. (S) However the March 28 elections turn out, Amir Peretz and the Labor Party are likely to have great influence, certainly more than they have had in the recent past. The PM's health problems also point in that direction. When Econoff posited to several economists the likelihood that Peretz could end up as Finance Minister in a government headed by Kadima/Sharon, they agreed that it was a very realistic scenario. They added that regardless of whether or not Peretz holds the Finance portfolio, his (mostly unknown) economic views will likely have great influence on the policies of the next government. Momi Dahan was very enthusiastic about the prospect. Daniel Doron, Director of the Israel Center for Social and Economic Progress, and a contributor to some of Netanyahu's reform plans, said it would be a "disaster." However, the consensus among those Econoff talked to (excluding Doron) was that Peretz is beginning to gather knowledgeable industrialists and economists around him, such as Avishai Braverman, the President of Ben Gurion University, and Benny Gaon, a respected businessman. Both Dahan and Bufman (of Bank Leumi) said that Peretz will quickly understand, once he is in a position of power, that there are limits to what he can change - the market will only allow him to go "so far, and no further." He will be constrained by the LGA terms and will not likely attempt to bust the budget framework. All agreed, however, that he would insist on drastic cuts in areas such as defense in order to finance considerably increased social spending.

Economic Reform Had to Happen

13. (S) Israeli society has experienced tremendous upheavals during the past two decades. First came the first intifada in the late 1980s, the mass immigration of about a million people from the former Soviet Union and Ethiopia, the Oslo Peace Process, and the hi-tech bubble. Then came the second intifada and the global hi-tech bust, both of which severely affected the Israeli economy, and forced changes in the old ways of doing things. Israel socialist heritage, the vestiges of which still maintained strict controls on foreign and domestic investment, and conferred enormous power on large unions and publicly-owned companies, had to give way to the modernized system that is being created by the reforms. Trade is Israel lifeline, as it has no resources other than its people. Without reforming its economy and opening it up to the world, it would not be able to compete.

Socialism Writ-Large is Dead

14. (S) With every upheaval, there are winners and losers. The losers, in this case those associated with the large unions, the kibbutzim, the large government-owned companies, and many who were simply raised on the ethos of "Socialist Zionism," have been fighting a rearguard action to maintain their influence. Exaggerating the issue of poverty is one of the weapons they have used. However, barring a return to violence, a continued economic recovery will eventually reach many of those who remain left behind. Regardless of the relative popularity of the populist Amir Peretz as the head of the Labor Party, the "poverty mongers" understand that the decline of the socialist ethos in Israel, which began with the Labor Party loss in the 1977 elections, is now very advanced - thus the severity of the reaction.

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